

**Access to Microfinance & Improved Implementation of Policy Reform
(AMIR Program)**

Funded By U.S. Agency for International Development

FACILITATION OF IPO'S

Draft Report

**Deliverable for Policy Component
Task No. 4.6.12
Contract No. 278-C-00-98-00029-00**

August 21, 2000

This report was prepared by Russell Diehl, in collaboration with Chemonics International Inc., prime contractor to the U.S. Agency for International Development for the AMIR Program in Jordan.

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REACH 2.0

Activity Name: 4.6.12 RoadMap Implementation

Capital and Financing

Scope of Work: Facilitation of IPO'S
Russell Diehl

Introduction

The REACH Initiative was developed in 1999 as a national strategy for Jordan to develop a vibrant, export-oriented Information Technology Services sector. The strategy's goal is to enhance Jordan's Information Technology sector and maximize Jordan's ability to compete in local, regional, and global markets.

The Consultancy task is to target the development of the business environment needed to facilitate Information Technology firms use of Initial Public Offerings on the Amman Stock Exchange. Laws and regulations must be adjusted in order that Information Technology firms can raise capital and "go Public" without requiring past records of profit, or other investment record criteria. In addition, certain new public 'registration' formats should be considered for adoption, which provide greater likelihood for success in the capital formation process by Information Technology firms.

The specific REACH objective is to: Establish the legal and regulatory environment conducive for the use of Initial Public Offerings in Jordan.

The IPO Community

In the Workshop held on August 7, 2000 the opening topic sought to identify the IPO community. The IPO Community includes the general user base such as high technology/ high growth (HT/HG) firms that are in need of and qualify for corporate equity financing in order to proceed with a well-developed business plan and business model. In addition, lawyers, accountants, and investment firms (broker-dealers), who will provide the professional and technical documentation, will join the HT/HG Company with support required by regulatory and capital market institutions.

Venture Capital organizations, while still nascent on Jordan, are also an important element in the IPO Community and project development process. They assist in the development of potential IPO candidates as investors.

The IPO team of lawyers, accountants and Investment firms all must contribute to the development of disclosure documentation and business rational for the IPO, which would be usually contained in a proper prospectus.

Attendees included: personnel from the Amman Stock Exchange, both management and broker/dealer members, business entrepreneurs and staff of private sector Information Technology companies in Jordan. Lawyers, accountants and other professionals associated with these support firms were also in attendance. Venture Capital professionals and other investors also contributed to the audience of approximately 95 people.

Findings

At the present moment neither the Companies Act nor the Securities Law of Jordan have a special Application-Registration for Initial Public Offerings. In consultation with attorneys at the esteemed Law firm of International Business Legal Associates (IBLAW), it has been suggested that Jordan adopt a "special" registration document designed for use by HT/HG companies wishing to raise capital by selling equity. The proposed Registration document would allow for unseasoned and seed stage companies to sell shares to the general Public with certain restrictions and disclosures. For example, investor suitability would include a statement from investors that they understand the risks and can sustain the loss if any without hardship. Also, there might be a limit to the amount of capital raised using this 'special' IPO Registration Document, similar to the Regulation 'A' Form and the S-18 Form used in the USA in the 1970's and 1980's.

A major hindrance to prospective LLC conversions to a Public Shareholding Company at this juncture is contained in the Companies Act. The essence of the regulation is that if a company is an existing LLC or similar entity and wishes to become a Public Shareholding Company it must demonstrate three years of consecutive profits, prior to 'going public' by being permitted to re-register as a Public Company. The anomaly is that a startup company can 'go public' without this compliance requirement. As a solution, there is of course the notion of simply to change the law to omit compliance with the profit requirement. This was recommended as an action item. On the other hand, private companies (LLC's) can be 'Acquired' by a 'new' Public Shareholder Company, which is legally proper and eliminates the need for the 3-year profit compliance. Changing laws can be very time consuming. Changing procedure is a matter of will.

In addition to a review of the Companies Act, an extensive review of the Securities Law as it relates to Capital Formation maneuvers was undertaken with the IBLAW. It was suggested and recommended that certain Directives, which have yet to be released to the public, be

'conditioned' for the IPO registration. An additional review of these Directives is anticipated in the coming weeks.

As a further observation, Venture Capital participants were vexed by the suggestion that IPO`s were not ready-made exits for their Funds, but rather simply a procedure for early round financing. Their disappointment in this view was outspoken. Nevertheless IPO`s are not and should not become an exit vehicle for any of the promotional investors, local or international. HT/HG companies need truly patient and 'smart' capital, which stays the course. The general failure to do so will risk, in short order, a taint of the IPO process. For the most part the Venture Capital industry in Jordan is in its early development. More long term and mature views on the topic are most surely to be recognized in due time.

Recommendations

Under current legislation, without requiring any changes in law or authority it is quite feasible to issue and float shares of Information Technology Companies on the Amman Stock Exchange.

In the case of both existing and "new" companies it was suggested that two features be considered. (1) All investors in IT-industry "IPO`s" be required to subscribe to the shares of an IPO with a Suitability Statement, which clearly determines an investor's suitability, or capability to sustain capital loss. (2) That each Registrant Company be required by a properly encharged authority (JSC, ASE) to have at least (50) fifty shareholders. The JSC or the ASE may simply require both of these suggestions, in order to comply with proper JSC registration and/or ASE trading compliance. The use of a suitability statement and the need for fifty shareholders need not involve legislative changes, but rather be Commission or Exchange Directives, simply even instructions.

As a final note, Jordan competes with many Emerging Economies from Asia and Eastern Europe, to Africa and Latin America. Stated concisely, what is it that The Kingdom of Jordan must do in order to become or stay competitive and attract Capital?

The Kingdom of Jordan Must:

I

Create a stable and predictable legislative environment.

II

Work on a flexible and resilient economic structure.

III

Invest in traditional *and* technological infrastructure.

IV

Promote private savings and domestic investment.

V

Develop aggressiveness on the international markets (exports) as well as attractiveness for foreign direct investment.

VI

Focus on quality, speed and transparency in government and administration.

VII

Maintain a relationship between wage levels, productivity and taxation.

VIII

Preserve the social fabric by reducing wage disparity and strengthening the middle class.

IX

Invest heavily in education, especially at the secondary level, and in the life-long training of the labour force.

X

Balance the economies of proximity and globality to ensure substantial wealth creation, while preserving the value systems that citizen's desire.

Initial Public Offerings (IPOs) Legal Overview

August 2000

Prepared by
International Business Legal Associates

LEGISLATION	RELEVANT PROVISION	COMMENTS	RECOMMENDATIONS
The Companies Law No. 22 of 1997	Article (217) A Limited Liability Company (LLC) may be transformed into a Public Shareholding Company (PSC) pursuant to the provisions stipulated in the Law. An application for transformation shall be submitted to the Companies Controller. This application shall include, <i>inter alia</i> , the approval of the LLC's General Assembly to the transformation, reasons for the transformation, The LLC's Balance Sheet for the last consecutive years preceding the application for transformation provided <i>that the average annual net profit in these years should not be less than 10% of the company's paid capital</i> , a statement indicating that the company's capital has been paid up in full, and <i>a statement by the LLC indicating the preliminary assessments of the value of its assets and liabilities</i> .	The requirement that any LLC intending to transform into a PSC must have three consecutive profitable years and that the average annual net profit in these years is no less than 10% of the LLC's paid capital constitutes a legal obstacle against the transformation of the Information Technology (IT) companies into PSCs, i.e., going public, and accordingly constitutes an obstacle against the growth of such companies.	Substitution of the three consecutive profitable years requirement with three audited fiscal years .
	Article (218) Upon submitting the Application for Transformation, the Minister of Industry & Trade may, upon the recommendation of the Controller, approve the transformation within 30 days as of the date of submitting the application after completing the following: 1. Valuation of the assets and liabilities of the LLC to be transformed <i>by a committee of experts and specialized persons</i> . The committee shall be formed by the Minister, provided that one member of the committee is a licensed auditor. The Minister determines the remuneration of the committee which shall be at the expense of the company. 2. The written approval of the LLC's creditors to the transformation.	Valuation of the LLC's assets and liabilities is carried out under the Law by a committee formed by the Minister of Industry & Trade. In practice, members of this committee are not sufficiently qualified to carry out this function. Accordingly, in many instances the valuation does not reflect the real value of the LLC's assets and liabilities.	Valuation process should be conducted by a private entity specialized and qualified in carrying out such function. Another approach would be to leave the valuation to the Company's Board of Directors and eventually whether the valuation is accurate or not would be governed by the market forces.
	Article (220) The transformation procedures shall come into effect only upon fulfilling the	A LLC transforming into a PSC must fulfill all the PSCs registration	

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	registration procedures of PSCs as stipulated in the Law.	requirements as a pre-requisite for such transformation. Accordingly, such requirements are examined hereunder.	
	Article (90) One. A PSC shall consist of a number of founders not less than two. Two. The Minister of Industry & Trade may approve that the PSC be established by one founder.	It is possible under the Law to establish a PSC by one founder subject to the Minister's approval.	
	Article (95) One. The authorized capital of the PSC shall not be less than JD 500,000 and the subscribed capital shall not be less than JD 100,000 or 20% of the authorized capital whichever is greater. Two. The non-subscribed capital shall be paid within 3 years as of the formation of the company.	For IT Companies to transform from LLCs into PSCs the minimum capital requirement of JD 500,000 is burdensome.	Creating a two-tier Public Shareholding Company registration where there would be a "Class B" Public Shareholding Companies with a minimum capital requirement of JD 250,000 and restrict the registration of such companies to certain types of economical activities such as IT Industry.
	Article (92) One. An Application for the Formation of the company shall be submitted by the founders to the Controller on the form designated for such purpose accompanied by other documents including, <i>inter alia</i> , the company's Articles of Association, Memo of Association. Two. The Articles of Association and Memo of Association shall include information including, <i>inter alia</i> , a statement of the shares in kind in the Company if any and the value thereof.	In the IT sector, shares in kind in the form of Intellectual Property Rights are very common. Therefore, the valuation of such is very essential in determining the capital of the company.	
	Article (97) The Company's shares may be in kind given against in kind offerings evaluated in cash in accordance with the provisions of this Law. Concession rights, patent rights and technical know-how and other	The Law recognizes IPR as in kind contributions in the PSC. The issue is in the valuation of such contributions.	

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	intangible rights are considered as payments in kind.		
	<p>Article (109)</p> <p>One. The founders of a PSC may offer, in exchange of their shares in the Company. Payments in-kind valued in cash. Concessions, patents, know-how and all intangible rights and any other rights approved by the founders shall be considered as payments in-kind. The Minister of Industry & Trade, upon the recommendation of the Controller, may ascertain the authenticity of evaluation of the payments in-kind in the manner he deems proper or by forming a committee of experts at the expense of the company provided that the committee submits its report within a maximum period of 60 days. After being approved by the Minister, the resolution of the committee shall be considered final. Should the founders object thereto, the Minister may refuse to register the company and non of the subsequent founders or shareholders may object to the value of the shares in-kind offered at the formation stage.</p> <p>Two. As for the shares in-kind offered at any stage subsequent to formation, the approval of the extra-ordinary General Assembly should be obtained on the value of the payments.</p>	<p>Formation Stage</p> <p>At the formation stage, the Minister may ascertain the value of the in-kind shares upon the recommendation of the Controller. The Law accords the Minister full discretion in terms of the manner of ascertaining the value of such shares including forming a committee. The norm is however, that the Minister forms a committee to determine the value. Usually the members of such committees are not sufficiently qualified to determine the value of in-kind shares such as IPR contributions and therefore affect the capital of the company.</p> <p>Moreover, under this provision, the committee's decision is deemed final and may not be objected by the founders. In addition, the committee's decision in terms of the valuation extends to subsequent founders and shareholders.</p> <p>Stages Subsequent to Formation</p> <p>Subsequent to formation, the value of in-kind shares is determined and approved by the company's extra-ordinary General Assembly.</p>	<p>The value of in-kind shares should be determined by the founders of the company at the formation stage. The extent of which such valuation is real and reflects the market value would be determined by the marker forces.</p>

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	<p>Article (100)</p> <p>One. Founders' shares in the PSC may not be disposed of prior to the lapse of at least 2 years from the formation of the company.</p> <p>Two. Transfer of founders' shares to heirs, between spouses, ancestors and descendants, and also among other founders and to third parties pursuant to a court order is allowed.</p>	<p>The two-year lock up period might constitute an obstacle to the growth of IT companies particularly in terms of Venture Capitalists involvement. In general, a Venture Capitalist investing in a company at the start-up level would like to have an exit mechanism available at any time. The lock-up period, although not long, may deter VCs from investing in IT companies at the start-up level.</p> <p>As the Law exists today, if a VC or any Angel Investor is willing to invest in a Privately-Held Corporation, in case such Corporation intends to go Public, the Investor would not be able to "exit" before at least five years, i.e., three years of consecutive profitable years and two years as a founder in the new Public Company.</p>	<p>The two-year lock-up period for founders should be cancelled or as a substitute, in case of a Class B PSC, this period may be cancelled. (<i>See</i> above for further details on Class B Corp.)</p>
	<p>Article (99)</p> <p>One. Upon signing the Articles of Association and Memo of Association of the PSC, the founders shall underwrite the entire value of the shares subscribed for by them and shall provide the Controller with evidence to this effect.</p> <p>Two. The shareholding of the founders of the PSC upon its formation shall not exceed 75% of the subscribed capital. The remaining shares shall be offered for subscription in accordance with the Securities Law.</p>	<p>The founders may only subscribe with up to 75% of the subscribed capital, the remaining part shall be offered in accordance with the Securities Law.</p>	
The Securities Law No. 23 of 1997	<p>Article (54)</p> <p>An issuer, an affiliate thereof, or an underwriter of either one of them shall not</p>	<p>All securities must be registered with the Commission prior to</p>	

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	offer any securities of the issuer before submitting the prospectus to the Jordan Securities Commission and paying the requisite fees.	offering thereof.	
	Article (55) An issuer, or an affiliate thereof, or an underwriter of either one of them shall not sell any securities owned by the issuer before the prospectus comes into effect, and unless the buyer has received the prospectus prior to the sale.	Before selling the securities, the prospectus must be approved and coming into effect. Moreover, each buyer must receive a copy of the prospectus prior to the sale.	
	Article (56) The prospectus shall contain the following information: One. A sufficient description of the issuer, the nature of its activities, and the persons in charge of its management from among members of its Board of Directors, executive officers, senior employees and major shareholders; Two. A sufficient description of the securities including a specification of their number, price and terms of issuance; a sufficient explanation of the risks involved in investing in such securities; an account of the uses of issue proceeds; and the amount of commissions which will be levied by persons involved in the issuance; Three. A clear statement of the financial position of the issuer and any relevant financial data including the balance sheet and profit and loss accounts for the last fiscal year, provided all statements are certified by an auditor. d. Any other information required or allowed by the Commission in accordance with the Instructions issued by the Board, and which may be of assistance to investors in making their decision regarding investing in the said securities.	The disclosure requirements under the Securities Law accord investors sufficient information regarding the issuer.	
	Article (59) a- An issuer shall submit to the		

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	<p>Commission annual and quarterly reports and shall proclaim such reports within the period set by the Board. The reports shall contain therein:</p> <ol style="list-style-type: none"> 1- The balance sheet; 2- The profit and loss account; 3- The cash flow statement; 4- The explanatory notes to the financial statements. <p>Two- Subject to the provisions of Paragraph (a) of this Article, the annual report shall contain the following:</p> <ol style="list-style-type: none"> 1- A sufficient description of the issuing company, and of the nature and areas of its activities; 2- The names of Board of Directors members, managers, senior employees and major shareholders; 3- Financial information certified by an auditor and showing the issuing company's financial position; 4- The management of issuer company assessment of future developments and prospects that may affect the company's business or its financial position. <p>c- All information referred to in the last two Paragraphs of this Article shall be considered insider information until proclaimed , and shall not be disclosed by the issuer company prior to proclamation .</p>		
	<p>Article (62) Prospectuses, periodical reports, information and data deposited with the Commission and which have already been proclaimed shall be accessible to the public for viewing and copying.</p>	<p>This accords investors access to information on each issuer and therefore accords them sufficient protection in making their investment decisions.</p>	
Issuance & Registration of Securities Instructions	<p>Article (4) Each issuer intending to issue securities shall submit to the Commission an</p>	<p>All issued securities must be registered with the Commission prior to</p>	

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No. 2 of 1997	application for the registration of such securities attached with the prospectus thereof prepared on the standard forms attached to the Instructions.	issuing such.	
	Article (6) One. Upon concluding the registration of securities procedures, the issuer may issue such securities by any of the following two means: 1. Public Offering. 2. Private Placement. Two. The provisions of Paragraph (a)(2) of this Article shall not apply to companies under establishment.	PSCs under establishment may only issue securities by means of Public Offering.	
	Article (7) A Public Offering shall be performed by means of a valid prospectus upon an announcement the text of which and the data and information included therein are approved by the Commission. Such announcement shall be published in two local newspapers at least twice at least seven days prior to the set date for commencement of subscription or sale.		
	Article (8) A Public Offering may be performed by any of the following two methods: One. Subscription in such securities by the public through licensed banks and financial companies. Two. Direct sale to public through the Dealing Room at the Amman Stock Exchange. Three. The provisions of Paragraph (b) of this Article shall not apply to companies under establishment until the Board of Commissioners issue a decision to the contrary.	Companies under establishment may only issue securities by means of Public Offering by public subscription through banks and financial companies only and not through the Amman Stock Exchange.	Companies Under establishment should be allowed to issue securities by means of Public Offering through the Amman Stock Exchange. The Board of Commissioner should issue a decision to this effect.
Listing of Securities on Amman Stock Exchange Instructions of 2000	Article (2) The Third Market is defined as that part of the Secondary Market where trading in unlisted securities is conducted.	Under these Instructions, a Third Market was created to allow companies to trade in their unlisted securities on this Market.	
	Article (20) a. A company shall file an application for trading in its securities through the Third Market subsequent to being granted the	A PSC upon being approved to commence its business may apply to the ASE for trading in its	

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	right to commence its business. The Company shall provide the ASE with the available financial statements and all information requested by the ASE.	securities through the Third Market. These Instructions came into force on June 15, 2000. The Third Market allows PSCs access to the Market and deal in its securities although such securities are not listed on the Stock Exchange. This provides the PSCs whose securities are not listed access to a liquid market. These Instructions positively affect the growth of PSCs.	
	Article (3) PSCs intending to list their securities on the Second Market must meet the following conditions: 1. The net shareholder equity shall not be less than 50% of the paid capital. 2. A full year must have elapsed since the PSC was granted the right to commence its business.		
	Article (5) PSCs the shares of which are transferred from the Second Market to the First Market shall fulfill the following conditions: C. The Company must have realized net pre-tax profits for at least two fiscal years out of the last three years.	This provision sets out an “investment” criteria for listing securities on the First Market. Such requirement is burdensome taking into account the nature of the IT companies in terms of profitability.	Such requirement should be substituted with a non-investment criteria, i.e., to have three audited finances for three fiscal years not necessarily profitable. The concerns regarding protecting investors are subdued by the Disclosure Requirements. The Company shall disclose its financial records to the public who will eventually decide whether it is proper to invest in such company or not. Accordingly, disclosure

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			requirements sufficiently protect the public and enables them to make a sound investment decision without burdening the companies by requiring profitable performance.
	<p>Article (21)</p> <p>Companies listed on ASE as well as Companies the shares of which are traded through the Third Market shall provide the ASE with the same statements and information that they supply to the Jordan Securities Commission and that are related to:</p> <p>One. Financial Statements</p> <p>Two. Information and decisions passed by such Companies which might affect the prices of securities issued by them.</p>	Such requirement affords investors trading on the Third Market sufficient protection in terms of being able to access information on companies they are intending to invest in.	
	<p>Article (23)</p> <p>The ASE Board of Directors shall be entitled to list the shares arising from privatization of PSCs and the shares resulting from the conversion of LLCs to PSCs directly on the First or Second Market on the condition that ASE is supplied with the statements and information it requests.</p>	<p>This provision accords the ASE Board of Directors discretion in allowing companies transformed from LLCs into PSCs to list their securities directly on the First or Second Market.</p> <p>In case of IT companies the majority of which are LLCs, in case such companies transform into PSCs they may be allowed to list directly on the First or the Second Market and therefore have access to a more liquid market than the Third Market.</p>	
	<p>Article (15)</p> <p>Jordanian issuers of securities wishing to list their securities on any stock exchange outside the Kingdom shall file an application with JSC through ASE including a report indicating the objectives of and justification for such listing. The</p>	Any Jordanian issuer intending to list its securities abroad must apply for the Commission for approval.	

LEGISLATION	RELEVANT PROVISION	COMMENTS	RECOMMENDATIONS
	listing application along with its attachments and the opinion of ASE shall be submitted for JSC for approval.		